



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

EIN: [REDACTED]  
[REDACTED]  
[REDACTED]  
[REDACTED]

Date: MAY 14 2002

DLN: [REDACTED]

Contact Person:

Tel:

Fax:

Dear Sir or Madam:

We have considered your application for recognition of exemption from Federal income tax under the provisions of section 501(c)(4) of the Internal Revenue Code of 1986 and its applicable Income Tax Regulations. Based on the available information, we have determined that you do not qualify for the reasons set forth in Enclosure I.

Consideration was given to whether you qualify for exemption under other subsections of section 501(c) of the Code and we have concluded that you do not.

As your organization has not established exemption from Federal income tax, it will be necessary for you to file an annual income tax return on Form 1041 if you are a trust or form 1120 if you are a corporation or an unincorporated association. Contributions to you are not deductible under section 170 of the Code.

If you are in agreement with our proposed denial, please sign and return one copy of the enclosed Form 6018, "Consent to Proposed Adverse Action". You have the right to protest this proposed determination if you believe that it is incorrect. If you protest, you should submit a written appeal giving the facts, law and other information to support your position as explained in the enclosed Publication 892, "Exempt Organizations Appeal Procedures for Unagreed Issues". The appeal must be submitted within 30 days from the date of this letter and must be signed by one of your principal officers.

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You may request a hearing with a member of the officer of the Regional Director of Appeals when you file your appeal. If a hearing is requested, you will be contacted to arrange a date for it. The hearing may be held at the Regional Office, or, if you request, at any mutually convenient District Office. If you are to be represented by someone who is not one of your principal officers, he or she must file a proper power of attorney and otherwise qualify under our Conference and Practice Requirements as set forth in Section 601.502 of the Statement of Procedural Rules. See Treasury Department Circular No. 230.

If you do not protest this proposed determination in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Code provides in part:

A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the district court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service.

If we do not hear from you within the time specified, this will become our final determination. In that event, appropriate State officials will be notified of this action in accordance with the provisions of section 6104(c) of the Code.

Sincerely Yours,

*Steven T. Miller*

Steven T. Miller  
Director, Exempt Organizations

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FACTS

The organization was incorporated on [REDACTED], under the laws of [REDACTED]

The Articles of Incorporation provide that the purpose of the organization:

"This Association does not contemplate pecuniary gain or profit to its members, and the purposes for which it is formed are to provide for maintenance, preservation architectural control and such other rights, duties and obligations provided in the Declaration of Covenants, Conditions, Easements and Restrictions [Convention Hotels] and any amendments, annexations and supplies thereto made in accordance with its terms, recorded in the Public Records of [REDACTED] (hereinafter referred to as the "Declaration") relating to or effecting the Property and the Common Property (as such terms are defined in the Declaration) within that certain real property located in [REDACTED], more particularly described in the Declaration, and such additional property as may be added thereto from time to time by annexation or otherwise as provided in the Declaration and in these Articles; and to insure the orderly development of the Property, and for these purposes the Association shall have the following powers:

- (a) To exercise all of the powers and privileges and to perform all of the duties and obligations of the Association as set forth in the Declaration, as the same may be amended from time to time as therein provided, said Declaration being incorporated herein as if set forth at length (capitalized terms which are not defined herein shall have the meaning set forth in the Declaration);
- (b) To fix, levy and collect (enforcing payment by any lawful means) all charges and assessments pursuant to the terms of the Declaration, as the same may be amended from time to time as therein provided, said Declaration being incorporated herein as if set forth at length (capitalized terms which are not defined herein shall have the meaning set forth in the Declaration);

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- (c) To purchase, receive, lease or otherwise own, hold, improve, build upon, operate, maintain, convey, sell, lease, transfer, dedicate for public use or otherwise dispose of real or personal property in connection with the affairs of the Association;
- (d) To borrow money, and with the approval of a Majority Vote, to mortgage or pledge any or all of its real or personal property as security for money borrowed or debts incurred;
- (e) To engage the services of agents, independent contractors or employees to manage, operate or perform all or any part of the affairs and business of the Association; and
- (f) To do and perform any and all lawful things and acts which in its discretion are necessary or desirable in carrying out any or all of the purposes for which the Association is formed, and pay the costs and/or expenses in connection therewith."

Article 6 of the Articles of Incorporation with regards to voting rights:

Class "A". Class "A" Members shall be all Owners, including the Declarant (as defined in the Declaration). Each Class "A" Member shall be entitled to one (1) vote per acre (rounded to the nearest acre) of Property owned by such Owner; provided, however, no Class "A" votes shall be exercised on account of any Property which is exempt from assessments under Section 8.5 of the Declaration..."

Class "B". The sole Class "B" Members shall be the Declarant, and shall be entitled to three (3) votes for each acre (rounded to the nearest acre) of Declarant's Property (as defined in the Declaration) owned by the Class "B" Member at the time any such vote is taken..."

Article 3 of the bylaws of the organization with regards to membership:

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Section 3.1 Membership. Every Owner shall be a "Member" of the Association. Membership shall be appurtenant to and shall not be separated from ownership of any Site..."

Section 3.2 Suspension of Membership. During any period in which a Member shall be in default in the payment of any annual, specific or special assessment levied by the Association, the right of such member to use any recreational facilities located on or within the Common Property and such Members right to vote in Association matters may be suspended by the Board until such assessment has been paid..."

Article 4 of the bylaws of the organization with regards to property rights in common property:

Section 4.1 Each Member shall be entitled to the use and enjoyment of the Common Property as provided in the Declaration.

Article 5 of the bylaws of the organization with regards to term of office:

Section 5.2 Directors During Class "B" Control Period. During the Class "B" Control Period and subject to the provisions of Section 5.3 of these Bylaws, [REDACTED] percent ( [REDACTED] %) of the directors shall be selected by the Class "B" Member acting in its sole discretion and shall serve at the pleasure of the Class "B" Member until the first to occur of the following:

- (a) fifty (50) years from the date of recording of the Declaration; or
- (b) when, seventy-five percent (75%) of the total developable acreage of Declarant's Property shall be sold by Declarant to third party owners, specifically provided, however, in determining said seventy-five percent (75%) of Declarant's Property all property which has been conveyed by Declarant to any Governmental Authority shall be excluded from the definition of Declarant's Property....

Section 5.5 Removal.

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- (a) When Declarant Does Not Hold Class "B" Membership. At any time that Declarant does not hold Class "B" Membership, the Members may remove any director from the Board, with or without cause, by vote at a duly noticed meeting or by action by written consent of a majority of the Members, so long as such notice, vote or action is taken in a manner provided elsewhere by these Bylaws and the Declaration. Notwithstanding the foregoing, the Members may not remove, without cause, a director who was a nominee of Declarant, or is an employee of Declarant, so long as Declarant owns any portion of Declarant's Property; provided, however, that the Members may remove any director for cause.
- (b) During Declarant's Class "B" Membership. During the time that Declarant holds Class "B" Membership, the Declarant may remove any director who is a nominee of Declarant, or an employee of Declarant. During the same time, the Members shall not have the power to remove any director who is a nominee of Declarant, or an employee of Declarant.

Article 1 of the Declaration of Covenant, Conditions, Easements and Restrictions with regards to common property:

- 1.12 "Common Property" shall mean any property, real or personal, tangible or intangible, legal or equitable, or otherwise owned by the Association, specifically including, but not limited to, rights of easement, right of way utilization agreements, licenses, occupation licenses and other rights and interests the Association may, from time to time, acquire and hold. The term shall include the Restricted Common Property as defined herein.

Article 3.3 of the Declaration of Covenant, Conditions, Easements and Restrictions with regards to Mass Easement System.

- 3.3.1 Interconnection Facilities. The Owner or Occupant of each Site shall, at Owner/Occupant's sole cost and expense, cause to be constructed any and all such facilities that are designed and approved by the Association.

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facilitating the interconnection and operation of any Mass Transit System which the Declarant or its designee shall operate from time to time. Each Owner or Occupant of the Site shall continuously maintain all Mass Transit System facilities upon such Site in a first-class manner consistent with the DCOG's.

3.3.2 Mass Transit System Operation and Maintenance.

The Declarant, for itself or its designee, reserves the right to be the exclusive operator of any and all Mass Transit System(s) upon the Property, as well as the right to make enhancements, changes, repairs thereto and provide maintenance thereof...."

3.3.3 Cooperation Regarding Mass Transit System. The

Declarant, the Association and each Owner shall cooperate with the Declarant, or its designee, and the agents and employees thereof, in the installation, construction, and maintenance of any Mass Transit System or Improvements related thereto.

Article 7 of the Declaration of Covenant, Conditions, Easements and Restrictions with regards to association powers and responsibilities.

7.1 Acceptance and Control of Common Property. The Association may acquire, hold, and dispose of tangible and intangible personal property and real property. The Declarant and its designees may convey to the Association improved or unimproved real estate located within the Property or Declarant's Property, personal property, leasehold and other property interests. Such property may be accepted by the Association and, if accepted, thereafter shall be maintained as Common Property by the Association at its expense for the benefit of its Members, subject to any restrictions set forth in the deed or other instrument transferring such property to the Association.

7.2 Maintenance of Common Property. The Association or its designees, subject to the rights of the Owners set forth in this Declaration, shall manage and control the Common Property and Improvements thereon (including, without limitation, common landscaped areas).

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keep it in good, clean, attractive, and sanitary conditions, order, and repair, consistent with this Declaration and the CPM Standard, as hereinafter defined, including, but not limit to:

- (a) all landscaping and other flora, parks, lakes, signage, structures, and Improvements, including any private streets, and bike and pedestrian pathways/trails, situated upon the Common Property;
- (b) landscaping, sidewalks, streetlights, and signage within the Common Property or public right-of-way within or abutting any Site, and landscaping and other flora within any public utility easement with the Declarant's Property but not within any Site (subject to the terms of any easement agreement relating thereto);
- (c) such portions of any additional property as may be included within the Common Property pursuant to this Declaration, any Supplemental Declaration, or any agreement for maintenance entered into by the Association;
- (d) all ponds, waterways, streams and/or wetlands located within the Property or Declarant's Property which serve more than one (1) Site or as a part of the drainage and storm water retention system for the Property or Declarant's Property, including any retaining walls, bulkheads, or dams (earthen or otherwise), and any fountains, lighting, pumps, conduits, and similar equipment installed therein or used in connection therewith, except to the extent that responsibility therefor has been assigned to or assumed by an Owner or Governmental Authority.
- (e) any property or facility owned by the Declarant and made available on a temporary or permanent basis, for the primary use and enjoyment of the Association and some or all of its Members, such property and facility to be identified by written notice from the Declarant to the Association and to be maintained by the Association until such time as Declarant revokes such arrangement.



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use and enjoyment by written notice to the Association.

- (f) Any property or facility used for a Mass Transit System or Improvements related thereto located on property owned by the Association or within a public right-of-way.

Article 8.6 of the Declaration of Covenant, Conditions, Easements and Restrictions with regards to exterior maintenance assessment.

8.6.1 Right to Maintain Exterior. In addition to maintenance of the Common Property, the Declarant or the Association may provide, after Notice, upon any Site requiring the same, when necessary in the opinion of the Declarant or the Association, to avoid blight, keep and preserve all improvements consistent with the DCOG's and this Declaration, and to preserve the beauty, quality, and value of the Property, maintenance, including paint, repair, roof repair and replacement, gutters, downspouts, exterior building surfaces, cleanup, maintaining, and landscaping.

Article 15 of the Declaration of Covenant, Conditions, Easements and Restrictions with regards to restricted common property.

- 15.1 Purpose. Certain portions of the Common Property may be designated as Restricted Common Property and reserved for the exclusive use or primary benefit of Owners. Occupants and invitees of Sites within a particular area. By way of illustration and not limitation, Restricted Common Property may include entry features, recreational facilities, landscape medians, cul-de-sacs, lakes and other portions of the Common Property within a particular area. The costs associated with maintenance, repair, replacement, and insurance of Restricted Common Property shall be assessed as an Assessment against the Owners of Sites in the area in which the Restricted Common Property is located.
- 15.2 Designation. Initially, the Declarant shall designate any Restricted Common Property. Such designation shall preclude the Association

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from later designating use of the same Restricted Common Property to additional property. Thereafter, a portion of the Common Property may be designated as Restricted Common Property of a particular area and Restricted Common Property may be reassigned upon approval of a Majority Vote of Members whose Sites are within the area(s) to which the Restricted Common Property is to be assigned. As long as the Declarant owns any property subject to this Declaration or has the right to subject additional property to this Declaration, any such assignment or reassignment shall also require the Declarant's approval.

- 15.3 Use by Others. The association may, upon approval of a Majority Vote of Members whose Sites are within the area(s) to which certain Restricted Common Property is assigned, permit Owners of Sites in other areas to use all or a portion of such Restricted Common Property upon payment of user fees, which fees shall be used to offset the CPM Costs attributable to such Restricted Common Property.

In the Part II Activities and Operational Information of Form 102+, you state:

"Common Area Maintenance - The association will maintain the common areas of the property. This includes landscaping, sidewalks, streetlights, signage within the common property, all ponds and waterways located within the property that services more than one site, and any property used for the Mass Transit System. This activity will promote a positive and enjoyable environment for patrons of the property as well as preserve the property value. This activity will be initiated in [redacted] and will represent about [redacted] percent of the Associations time. This activity will be conducted by [redacted] in [redacted], [redacted]."

"Declaration Enforcement - The Association will enforce the declaration (attached) set forth by the Declarant. This activity will ensure that the owners maintain the integrity of the appearance of the property. In addition, it will also assist with the preservation of the value of the property."

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In your response dated [REDACTED], you state:

"[REDACTED] consists of multiple single development private real property owners within a [REDACTED] acre planned commercial development. (No residential component is envisioned)."

LAW AND ANALYSIS

Internal Revenue Code Section 501(c)(4) of the Code provides for the exemption from Federal income tax of civil leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare

Internal Revenue Code Section 1.501(c)(4)-1(a)(2)(i) of the regulations states that an organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the people of the community. An organization existing within the scope of this section is one that is operated to bring about civic betterment and social improvements.

In Rancho Santa Fe Association, v. United States Of America, 589 F. Supp. 54, the court considered the issue of whether the development was an organization operated exclusively for the promotion of social welfare such that it was exempt from federal income tax under Section 501(c)(4). The court held that the development fell within the definition of a tax-exempt organization devoted to the promotion of the general welfare. It also held that the organization performed the functions of a governmental entity and brought about civic betterments and social improvements that would be sorely missed by the community should they be lost or curtailed. Lastly, it held that the development served as a liaison to larger governmental entities to protect the interests of the community that it represented.

Revenue Ruling 69-280 provides the organization must be performing services that its members would otherwise have to provide for themselves. It is a private cooperative enterprise for the economic benefit or convenience of the members. In Commissioner v. Lake Forest, Inc., 305 F. 2d 814 (1962), the court held that a corporation that provided housing on a cooperative basis lacked the necessary requirements of an organization described in section 501(c)(4) of the Code. The court

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operation to be a private self-help enterprise with only an incidental benefit to the community as a whole.

Similarly, in the case described in Revenue Ruling 69-280, it was held that the organization is operated primarily for the private benefit of members. Any benefits to the community are not sufficient to meet the requirement of the regulation that the organization be operated primarily for the common good and general welfare of the people of the community. Accordingly, this organization is not exempt from Federal income tax as a social welfare organization under section 501(c)(4) of the Code.

Revenue Ruling 74-99 provides that for a homeowners association to qualify for exemption under section 501(c)(4) of the Code, it needs to satisfy three requirements. The association must serve a "community" which bears a reasonable recognizable relationship to an area ordinarily identified as governmental. The association must not conduct activities directed to the exterior maintenance of private residences. The common areas or facilities it owns and maintains must be for the use and enjoyment of the general public. Revenue Ruling 72-102 was modified.

Revenue Ruling 78-86 provides the Corporation was formed by a group of local merchants to establish and operate a public off-street parking facility in order to alleviate a lack of parking space in the central business district of Monterey. Anyone could park a car at this facility for 25¢ per hour. However, in order to provide their customers with free parking while they shopped the participating merchants set up a validation stamp system. Under this system, customers could present their parking vouchers to participating merchants and obtain parking stamps instead of paying cash for parking. The merchants purchased the stamps in books of 100 at \$18 per book. Since each stamp permitted one hour of parking, merchants were in effect paying 18¢ for each hour of free parking for their customers.

A parking arrangement whereby merchants join together to provide parking for their customers at a reduced rate serves the merchants' private interests by encouraging the public to patronize their stores. Rather than providing their own parking, merchants are able to join together to provide a parking facility in which all share the benefits.

Thus, although there may well be some public benefit from the construction and operation of the parking facility,

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be said to be operated exclusively for charitable purposes under section 501(c)(3) of the Code or primarily for social welfare purposes under section 501(c)(4). Further, providing parking in a manner similar to that in Monterey is carrying on a business with the general public in a manner similar to organizations that are operated for profit. Such trade or business does not further exempt purposes under either section 501(c)(3) or (4).

GOVERNMENT'S POSITION

Your organization is not exempt under Section 501(C)(4) of the Internal Revenue Code. Your organization is similar to the organization described in Revenue Ruling 74-99 because your organization consists of multiple single development private real property owners within a [REDACTED] acre planned commercial development. Membership in the association is required of all purchasers of lots in the development. Membership is open only to those who purchase lots. The organization is supported by periodic assessments against the members and an unpaid assessment constitutes a lien on the property of the member. The stated purposes of the organization are, generally speaking, to administer and enforce covenants for preserving the architecture and appearance the property, and to maintain common areas.

Your organization is also similar to the organization described in Revenue Ruling 69-280. Section 8.6.1 of the Declaration of Covenants, Conditions, Easements and Restrictions allows the Declarant [REDACTED] or the Association to provide the services of maintenance. This includes paint, repair, etc., when necessary in the opinion of the Declarant or the Board "to avoid blight, keep and preserve all improvements consistent with the DCOG's and this Declaration, and to preserve the beauty, quality, and value of the property."

Likewise, as with Revenue Ruling 78-86, your organization is formed by a group of commercial/business property owners to maintain the common areas of the businesses in order to attract customers to their businesses while the customers are staying at the hotels or golfing at the golf course.

You cite Rancho Santa Fe Association, v. United States of America, 589 F. Supp. 54. The court held that the organization performed the functions of a governmental entity and was not about civic betterments and social improvements that would

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sorely missed by the community should they be lost or curtailed. Your organization is not performing the functions of a governmental entity for the general public. The court held that the development served as a liaison to larger governmental bodies to protect the interests of the community that it represented. Your "community" consists of a commercially zoned sector of a city that lacks a permanent residential presence, and identity as a community within the city. You are a business park.

TAXPAYER'S POSITION

On page 2 of your response dated [REDACTED] you state in support of your position that you are exempt under Section 501(c)(4) of the Internal Revenue Code:

"As you know, Revenue Ruling 69-280 focuses upon an organization incorporated for the purpose of providing specified services for homeowners in a housing development which included maintaining exterior walls and roofs of the individual home units. In our Association, Section 8.6.1 of the Declaration allows the Declarant [REDACTED], a [REDACTED] corporation) or the Association to provide the services of maintenance, including paint, repair, etc., when necessary in the opinion of the Declarant or the Board "to avoid blight, keep and preserve all improvements consistent with the DCOG's and this Declaration, and to preserve the beauty, quality, and value of the property." However, this power is giving to the Declarant and the Association in order to enforce the covenants. There is no private benefit conferred upon a member because the member must reimburse the Association for these services or subject their property to liens and a foreclosure, as well as a suspension of their membership."

"Your analysis also seems to indicate that the Association is not be serving a "community" Revenue Ruling 74-22 and Revenue Ruling 72-102 note the following:

For the purposes of section 501(c)(4) of the Code, a neighborhood, precinct, subdivision, or housing development may constitute a community. For example, tennis and athletic leagues in urban areas have traditionally represented neighborhoods or other subparts of much larger political units. By administering and enforcing covenants, and coming and maintaining certain non-residential, primarily commercial properties of the type normally maintained by municipal governments, this organization

[REDACTED]

Revenue Ruling 72-102 points out that even though an organization may be established by a developer and its existence may have aided him in selling housing units, any benefits to the developer and its existence may have aided him in selling housing units, any benefits to the developer are merely incidental. Also, even though the activities of the organization serve to preserve and protect property values in the community, these benefits that accrue to the property owner-members are likewise incidental to the goal to which the organization's activities are directed, the common good of the community.

Finally, your analysis cited Commissioner v. Lake Forrest, Inc. for the general principle that a private self-help enterprise with only an incidental benefit to the community as a whole, lacks the necessary requirements of an organization described in Section 501(c)(4) of the Code. However, in that case, the corporation was formed to assist veterans in purchasing project housing. The court noted numerous facts which prevented the corporation from obtaining 501(c)(4) status, including the fact that the corporation's organizational documents did not expressly stipulate that the corporation was not organized for profit. I would cite Pancho Santa Fe Association v. United States of America, 759 F. Supp. 54(1984) for a much more recent and analogous case of a homeowners association seeking 501(c)(4) exemption status."

in your disagreement with the use of Revenue Ruling 68-609, [REDACTED]  
[REDACTED] in our Association, [REDACTED]  
[REDACTED] Declaration [REDACTED]  
[REDACTED] a [REDACTED] corporation) or the Association to [REDACTED]

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services of maintenance, including paint, repair, etc., when necessary in the opinion of the Declarant or the Board "to avoid blight, keep and preserve all improvements consistent with the DCOG's and this Declaration, and to preserve the beauty, quality, and value of the property." You furthermore state, "There is no private benefit conferred upon a member because the member must reimburse the Association for these services or subject their property to liens and a foreclosure, as well as a suspension of their membership."

Revenue Ruling 69-280 held that the organization was incorporated as a nonprofit membership corporation for the purpose of providing specified services for the homeowners in a housing development. The services consist of maintenance of the exterior walls and roofs of the individual home lots. This includes, for example, painting of exterior walls and repair of roofs. If a person purchases a unit in the housing development, he is required to become a member of the organization. The organization is supported entirely by annual dues charged to members. The dues are based on the estimated expenses of the organization plus an amount for reserves to cover large expenditures, such as the replacement of roofs. Revenue Ruling 69-280 also provides that the organization so described is performing services that its members would otherwise have to provide for themselves. It is a private cooperative enterprise for the economic benefit or convenience of the members.

Your activities and purposes are similar to those described in the Revenue Ruling because your organization is performing services that its members would otherwise have to provide for themselves and the dues are based on the estimated expenses of the organization plus an amount for reserves to cover the expenditures.

You state "The principal reason for the Association's maintenance and control of the Common Property is to protect the taxpayers in Revenue Ruling 72-102, Revenue Ruling 74-99 and Revenue Ruling 80-63... Maintenance of these common areas... the restrictions contained in the Declarations... of the community and also lessen the burdens of... However, your organization is also similar to Revenue Ruling 72-102, 74-99 and 80-63 as your organization is performing services that the members would otherwise have to provide for themselves. The organization is primarily dedicated to the members with incidental benefits to the general public in significant lessening of the burdens of government."



[REDACTED]

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#### CONCLUSION

Your organization is engaged in activities that are of primary benefit to the members of [REDACTED] organization. Furthermore, your organization is not operated exclusively for the promotion of social welfare. You do not qualify for exemption from federal income tax as a social welfare organization under section 501(c)(4) of the Code.